

TAX COMMENTARY

The Trustee is unable to provide any advice as to the tax treatment of payments received out of the BCFRT.

The Trustee is able to offer the following *general* comments on considerations that might be applicable in determining the tax status of a specific mitigation payment. However, each recipient will have to make his, her or its own determination as to the tax status of any specific payment. Tax status may vary from payment to payment and from recipient to recipient.

Income Tax Considerations For Contractors

To the extent that the BCFRT has income, the BCFRT will issue a T3 slip to recipients. The amount shown in the T3 slip will be included in the income of the recipient. The issue will then be whether the recipient can claim an offsetting deduction for some expense incurred by the recipient (such as the making of a severance payment to employees of the recipient). The BCFRT will attempt to issue T3 slips only in respect of mitigation payments that are used to fund severance or other deductible amounts.

To the extent that a payment is not covered by a T3 slip, the payment might have the status of income or capital for the recipient. Income receipts must be included in income. Capital receipts might have to be reflected through an adjustment to the adjusted cost base of capital property or as proceeds of disposition of that property.

To the extent that a payment is not otherwise included in income, an issue might arise as to whether the payment is a form of assistance under paragraph 12(1)(x) of the Income Tax Act. If paragraph 12(1)(x) applies, the payment must be included in income except to the extent that the payment is applied to reduce an otherwise deductible amount or to reduce the cost of property.

The above comments are provided for information only, and cannot be considered to be tax advice. Each recipient of mitigation funds from the BCFRT should seek the advice of their own accounting or legal advisors.

Income Tax Considerations for Employees

To the extent that a mitigation payment is used to fund a severance payment made to an employee, the employee will likely be taxable on the severance payment.

Normal RRSP Contribution Room

Employees can contribute severance payments to a registered retirement savings plan (an “RRSP”) and deduct the amount of the contribution from income for tax purposes. In 2005, the deductible amount is limited to the *lesser* of the following two amounts:

- (a) \$16,500; and

- (b) 18% of “earned income” realized in the preceding taxation year (in this case, 2004).

The above deduction limit is increased by any unused RRSP deduction room carried forward from 1991 and subsequent taxation years.

Assessments issued in respect of 2004 income tax returns will indicate the amount of normal RRSP contribution room for 2005.

Additional RRSP Contribution Room

Certain employees might be able to contribute additional amounts to an RRSP. Generally, this additional contribution room is available only to persons who were employees prior to 1996. Such employees can contribute the following additional amounts:

- (a) \$2,000 for each year of employment prior to 1996; plus
- (b) for years prior to 1989 during which the employer made *no* contributions on the employee’s behalf to a pension plan or deferred profit sharing plan, an additional \$1,500.

The additional contribution room does not affect the normal contribution room referred to above.

Assessments issued in respect of 2004 income tax returns would not generally indicate whether this additional RRSP contribution room is available.

Source Deductions

Any portion of the severance payment that is not sheltered from source deductions as a result of being directed by the employer into the ex employee’s RRSP, or spousal or common law partner RRSP, will normally be subject to source deductions for income tax at the following rates:

- 10% on amounts up to \$5,000
- 20% on amounts from \$5,000 to \$15,000; and
- 30% on amounts over \$15,000

Depending on other income during the year, recipients may have to pay additional tax on the above amounts when they file their returns. However, if the recipient’s total earnings received or receivable during the calendar year, including the lump-sum severance payment, are less than the “claim amount” on the employee’s Personal Tax Credit Return (Form TD1), no income tax source deduction need be made.

No source deductions are to be made for CPP or EI on severance payments.

Goods and Services Tax

If a payment is subject to GST, the payment is to be treated as a GST-included amount. This means that the recipient of the payment will be considered to have collected 7/107 of the payment as GST and will be obligated to remit 7/107 of the payment as GST collected. The remittance obligation is subject to any offsetting input tax credit claim that the recipient might have in respect of GST paid by the recipient on business inputs.

The BCFRT has submitted a ruling request to the Canada Revenue Agency on the status of mitigation payments for GST purposes. Once the ruling is issued, details of the ruling will be posted on this web site. However, the Canada Revenue Agency will consider itself bound by the ruling only in respect of the BCFRT and not in respect of any other entity.

Disclaimer

As noted, the above comments are intended as general commentary only. The BCFRT is unable to provide any specific tax advice. Accordingly, recipients should consult with their own advisers.